

D.T.E. 00-25

Joint petition of Fall River Gas Company and Southern Union Company for approval of merger.

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## I. INTRODUCTION

On January 27, 2000, Fall River Gas Company ("Fall River") and Southern Union Company ("Southern Union") (collectively, "Petitioners"), filed with the Department of Telecommunications and Energy ("Department") a petition for approval, pursuant to

G.L. c. 164, § 96, of the merger of Fall River with and into Southern Union (Petition at 5). Moreover, the Petitioners requested that the Department confirm that Southern Union, as the surviving corporation of the merger, would continue to have all of the franchise rights and obligations currently held by Fall River without having to secure approval of the Massachusetts General Court pursuant to G.L. c. 164, § 21 (*id.*). The Department docketed this matter as D.T.E. 00-25.<sup>(1)</sup>

Pursuant to notice duly issued, the Department conducted a public hearing in Fall River on April 11, 2000 to afford interested persons the opportunity to comment on the proposal. The Attorney General of the Commonwealth ("Attorney General") intervened as of right pursuant to G.L. c. 12, § 11E. The Department granted the Division of Energy Resources limited participant status in this proceeding.<sup>(2)</sup>

On June 2, 2000, the Department held an evidentiary hearing.<sup>(3)</sup> The Petitioners presented the testimony of three witnesses: (1) Peter H. Kelley, president and chief operating officer of Southern Union; (2) Ronald J. Endres, executive vice president and chief financial officer of Southern Union; and (3) Peter H. Thanas, senior vice president and treasurer of Fall River. On June 20, 2000, the Petitioners submitted a brief reaffirming

their positions. The evidentiary record consists of 82 exhibits and responses to seven record requests.

Fall River is a local distribution company ("LDC") supplying natural gas to approximately 47,843 customers in the city of Fall River and towns of Somerset, Swansea, and Westport (Exhs. SUFR-3, at 3; DTE 2-9, at 3-4). Southern Union is a multistate LDC incorporated in Delaware with a principal place of business in Austin, Texas, supplying natural gas to approximately 1.2 million customers through four operating divisions in Florida, Missouri, Pennsylvania, and Texas (Exh. SUFR-1, at 2-3).

## II. DESCRIPTION OF PROPOSAL

### A. Structure of Merger

The Petitioners request Department approval of an Agreement of Merger ("Merger Agreement") that would reorganize Fall River as a Massachusetts operating division of Southern Union (Exh. SUFR-5, at § 2.1). Under the terms of the Merger Agreement, Fall River will merge directly with and into Southern Union; Southern Union as the surviving corporation would operate Fall River as a separate division ("Fall River Division") (id.; Exh. DTE 2-37).<sup>(4)</sup>

The Petitioners propose that, upon Fall River's merger with Southern Union, each outstanding Fall River share would be converted into (i) an equivalent number of Southern Union shares determined by dividing \$23.50 by the average market price of Southern Union common stock prior to the closing of the merger, subject to certain adjustments ("Exchange Ratio"),<sup>(5)</sup> or (ii) upon election of the shareholder, the right to receive cash without interest, subject to certain limitations, all such that no more than 50 percent of the total consideration paid by Southern Union is in cash (Exh. SUFR-5, at 2; Tr. at 76).<sup>(6)</sup> In accordance with standard generally accepted accounting principles ("GAAP"), the Petitioners intend to account for the transaction through purchase accounting, whereby Southern Union would record the difference between the purchase price and the sum of Fall River's tangible and intangible assets, less liabilities, as a plant acquisition adjustment (Tr. at 84). The Petitioners stated that the votes required under G.L. c. 164, § 96 from the shareholders of both Fall River and Southern Union were scheduled to take place later in the summer of 2000 (Tr. at 78-79).

### B. Costs Associated With Merger

The Petitioners project that the costs associated with the merger would be approximately \$39.95 million. This projection includes: (1) \$36.95 million in acquisition premiums associated with the difference between the price paid by Southern Union for Fall River and book value of the respective regulated utility assets acquired, and (2) approximately \$3,000,000 in transaction costs, including legal, accounting, and financial expenses (Exhs. DTE 2-13; DTE 4-9). The transaction costs consists of approximately \$2,500,000 in legal and related expenses, and approximately \$500,000 in post-merger expenses

### C. Rate Plan

After the proposed merger, Fall River's current base rates would remain in effect (Exh. SUFR-2, at 19; Tr. 1, at 46).<sup>(7)</sup> In lieu of proposing to recover merger-related costs in this proceeding, Southern Union requests the opportunity to develop, for filing in a future proceeding, a proposal to establish a Performance Base Rate ("PBR") approach for setting rates for the Fall River Division (Exhs. SUFR-2, at 18; DTE 2-23). In the event the Department does not approve the future filing of a PBR, the Petitioners request that the Department recognize Southern Union's right to seek recovery of merger-related costs, including the acquisition premium, in a future ratemaking proceeding to the extent that savings are demonstrated to have resulted from the merger (Exh. SUFR-2, at 18; Tr. at 10-11, 40-44).

### III. STANDARD OF REVIEW

The Department's authority to review and approve mergers and acquisitions is found at G.L. c. 164, § 96, which, as a condition for approval, requires the Department to find that mergers and acquisitions are "consistent with the public interest". In Boston Edison

Company, D.P.U. 850, at 6-8 (1983), the Department construed § 96's standard of consistency with the public interest as requiring a balancing of the costs and benefits attendant on any proposed merger or acquisition. The Department stated that the core of the consistency standard was "avoidance of harm to the public." Boston Edison Company, D.P.U. 850, at 5. Therefore, under the terms of D.P.U. 850, a proposed merger or acquisition is allowed to go forward upon a finding by the Department that the public interest would be at least as well served by approval of a proposal as by its denial. Boston Edison Company, D.P.U. 850, at 5-8; NIPSCO-Bay State Acquisition at 9 (1998); Eastern-Essex Acquisition, D.T.E. 98-27, at 8 (1998). The Department has reaffirmed that it would consider the potential gains and losses of a proposed merger to determine whether the proposed transaction satisfies the § 96 standard. NIPSCO-Bay State Acquisition at 9 (1998); Eastern-Essex Acquisition at 8; Boston Edison Company, D.P.U./D.T.E. 97-63, at 7 (1998); Mergers and Acquisitions, D.P.U. 93-167-A at 6, 7, 9 (1994). The public interest standard, as elucidated in D.P.U. 850, must be understood as a "no net harm," rather than a "net benefit" test.<sup>(8)</sup> Eastern-Essex Acquisition at 8. The Department considers the special factors of an individual proposal to determine whether it is consistent with the public interest. Eastern-Essex Acquisition at 8; D.P.U./D.T.E. 97-63, at 7; Mergers and Acquisitions at 7-9. To meet this standard, costs or disadvantages of a proposed merger must be accompanied by offsetting benefits that warrant their allowance. NIPSCO-Bay State Acquisition at 10; Eastern-Essex Acquisition at 8; D.P.U./D.T.E. 97-63, at 7; Mergers and Acquisitions at 18-19.

Various factors may be considered in determining whether a proposed merger or acquisition is consistent with the public interest pursuant to G.L. c. 164, § 96. These

factors were set forth in Mergers and Acquisitions: (1) effect on rates; (2) effect on the quality of service; (3) resulting net savings; (4) effect on competition; (5) financial integrity of the post-merger entity; (6) fairness of the distribution of resulting benefits between shareholders and ratepayers; (7) societal costs, such as job loss; (8) effect on economic development; and (9) alternatives to the merger or acquisition. NIPSCO-Bay State Acquisition at 10; Eastern-Essex Acquisition at 8-9; D.P.U./D.T.E. 97-63, at 7-8; Mergers and Acquisitions at 7-9. This list is illustrative and not exhaustive, and the Department may consider other factors when evaluating a § 96 proposal. NIPSCO-Bay State Acquisition at 10; Eastern-Essex Acquisition at 9; Mergers and Acquisitions at 9.

With respect to the recovery of acquisition premiums, the Department has found that if a petitioner can demonstrate that denial of recovery of an acquisition premium would prevent the consummation of a particular merger that otherwise would satisfy G.L. c. 164, § 96, then the Department may be willing to consider recovery of an acquisition premium.<sup>(9)</sup> Eastern-Essex Acquisition at 9; Mergers and Acquisitions at 18-19. The Department will determine whether an acquisition premium should be allowed in a specific case by applying the general balancing of costs and benefits under the § 96 consistency standard. NIPSCO-Bay State Acquisition at 10-11; Eastern-Essex Acquisition at 9; Mergers and Acquisitions at 18-19. Thus, allowance or disallowance of an acquisition premium would be but one part of the cost/benefit analysis under the § 96 consistency inquiry. NIPSCO-Bay State Acquisition at 11; Eastern-Essex Acquisition at 9; Mergers and Acquisitions at 7.

The Department's determination whether the merger or acquisition meets the requirements of § 96 must rest on a record that quantifies costs and benefits to the extent that such quantification can be made. NIPSCO-Bay State Acquisition at 11; Eastern-Essex Acquisition at 10; Mergers and Acquisitions at 7. A § 96 petitioner who expects to avoid an adverse result cannot rest its case on generalities, but must instead demonstrate benefits that justify the costs, including the cost of any premium sought. NIPSCO-Bay State Acquisition at 11; Eastern-Essex at 10; Mergers and Acquisitions at 7. This admonition is particularly apt where allowance of an acquisition premium is sought. NIPSCO-Bay State Acquisition at 11; Eastern-Essex Acquisition at 10; Mergers and Acquisitions at 7.

#### IV. SPECIFIC CONSIDERATIONS OF THE MERGER

In considering the Petitioners' proposal, the Department's analysis focuses on the following: (1) effect on rates and resulting net savings; (2) effect on the quality of service; (3) societal costs; (4) acquisition premium; (5) financial integrity of the post-merger gas company; (6) effect on competition and economic development; (7) cost allocation issues; and (8) jurisdictional issues concerning Southern Union's operation of Fall River as a division of Southern Union.

##### A. Rates and Resulting Net Savings

###### 1. Effect on Rates

a. Petitioners Proposal

The Petitioners propose to maintain Fall River's present base rates after the merger. While they have not requested recovery of the acquisition premium or merger-related costs in this proceeding, the Petitioners request permission to propose a PBR approach for setting rates for the Fall River Division as part of a future proceeding. Alternatively, the Petitioners request that the Department recognize Southern Union's right to seek recovery of merger-related costs, including the acquisition premium, in a future ratemaking proceeding to the extent that savings are demonstrated to have resulted from the merger (Exh. SUFR-2, at 18; Tr. at 10-11).

The Petitioners contend that the merger will not adversely impact the rates charged to customers, and that any future changes to base rates would remain subject to Department investigation and approval (Petitioners Brief at 10). Absent the merger, the Petitioners claim that Fall River would have requested a rate increase of approximately \$2,000,000 in the year 2000 (*id.*)<sup>(10)</sup>

b. Analysis and Findings

The Petitioners contend that, absent the merger, Fall River would have submitted a § 94 rate filing during 2000. The record in this case demonstrates that Fall River has filed base rate cases approximately every five years.<sup>(11)</sup> Based on both the timing and level of base rate increases granted historically through fully-adjudicated proceedings and settlements, the Department finds that the Petitioners have provided a conservative estimate of what Fall River may have sought in a base rate proceeding filed this year. Accordingly, the Department finds that the merger would serve to defer some level of rate increase that would otherwise have been borne by Fall River's ratepayers. Therefore, we conclude that Fall River's ratepayers would be at least as well off with the merger than they would be absent the merger. NIPSCo-Bay State Acquisition, D.T.E. 98-31 (1998).

The Petitioners have represented that they are not seeking approval of a rate recovery mechanism as a component of their merger proposal. Rather, the Petitioners seek approval to file a rate recovery mechanism in a future rate proceeding, either in the form of a PBR or through a demonstration of merger-related savings. Section § 94 mandates the mechanism by which gas, electric, and water companies may petition the Department for a change in rates and the procedures for the Department to follow in reviewing any proposed rate change. Moreover, § 94 provides that the Department, on its own motion, may commence an investigation of a filed rate. The Department has broad discretion in exercising its authority to regulate rates under G.L. c. 164, § 94. See American Hoechst Corp. 379 Mass. 408, 411, 412, 413 (1980) (Department free to select or reject particular method of regulation as long as choice not confiscatory or otherwise illegal). The Department's actions under § 94 have been accorded deference in the realm of economic regulation. See, e.g., Massachusetts Oilheat Council, 418 Mass. at 802-807 (1994). Therefore, the Department concludes that there is no express or implied language in § 94 that would limit the Department to a particular regulatory scheme or its specific duration. Accordingly, we find that the Petitioners' proposal is consistent with the discretion



afforded the Department under these statutory provisions. Eastern-Essex Acquisition at 15-16.

Nonetheless, in Incentive Regulation, D.P.U. 94-158, at 65-66 (1995), the Department directed utilities to submit PBR proposals in future base rate cases, and if they failed to do so, explain the reasons for such a failure and demonstrate, with full specificity, how they would be seeking to achieve more efficient operations, better cost controls, and lower rates. See also Fitchburg Gas and Electric Light Company, D.T.E. 98-51, at 5-7 (1998). Therefore, the Department directs Southern Union to submit an incentive-based proposal as part of its next base rate filing for its Fall River Division. Southern Union and its shareholders are placed on notice that they bear the burden to demonstrate the propriety of its proposed PBR filing, and bear the risk as to whether incentive regulation will provide sufficient revenues to offset the acquisition premium and transaction costs arising from this merger.

## 2. Synergistic Savings

### a. Introduction

The Petitioners state that although Southern Union pursued a merger with Fall River primarily for strategic purposes, cost savings will be realized over the long term as a result of the merger (Exhs. SUFR-1, at 9-10; SUFR-2, at 13-14). The Petitioners estimate that there is a potential for net annual merger-related savings to Fall River of \$105,836 related to "public company functions" consisting of: (1) \$38,456 in directors fees; (2) \$18,250 in shareholder services; (3) \$32,875 in financing fees; and (4) \$18,047 in gas association dues, partially offset by a slight increase of \$1,792 in rating agency fees that would be allocated to the Fall River Division (Exh. SUFR-2, at 14-15; Exh. RJE-3).

According to the Petitioners, the merger of Southern Union with Fall River would expand the geographic diversity of Southern Union's operations by adding New England to its southwest, southeast, and mid-Atlantic regions, thereby reducing the effect of adverse economic or weather conditions in a particular part of the country on Southern Union's revenues, with resulting benefits to the Fall River Division (Exhs. SUFR-1, at 9-10; SUFR-2, at 13-14). Moreover, the Petitioners state that Southern Union and Fall River share similar business perspectives, thereby providing the opportunity for both to improve upon their present operations by drawing from each other's strengths (Petitioners Brief at 14).

### b. Analysis and Findings

In order to recover merger-related costs, a petitioner must demonstrate the quantified costs and benefits to the extent that such quantification can be made, as well as demonstrate benefits that justify the costs; a petitioner cannot rest its case on generalities. Eastern-Colonial Acquisition at 7; NIPSCO-Bay State Acquisition at 11; Eastern-Essex Acquisition at 10; Mergers and Acquisitions at 7. While the Petitioners claim that cost savings will be available over the long term as a result of the merger, the Petitioners have

provided no projected savings values to the Department (see, e.g., Exhs. DTE 2-40, DTE 2-41; DTE 3-1, DTE 3-2). While they also claim that the merger of Fall River will expand Southern Union's geographic diversity and thereby reduce the effect on Southern Union's revenues of adverse economic or weather conditions in a particular part of the country, the Petitioners provided no proven direct causal link with savings. Stating that a merger is based on strategic considerations does not absolve a company from providing the quantitative evidence necessary to determine the propriety of a § 94 filing.

Although the Petitioners have listed annual savings of approximately \$105,000 related to the reduction of duplicative processes between Southern Union and Fall River, they have failed to show sufficient savings to recover the merger-related costs of approximately \$39.95 million over what could reasonably be considered as a recovery period. Accordingly, the Department finds that the Petitioners have failed to provide adequate evidence that savings equal or exceed the costs to be recovered.

Despite the present lack of showing concerning premium recovery, the merger has been structured so that Fall River's ratepayers are not at risk for recovery of any acquisition premium or merger-related costs until Southern Union files for a PBR proposal for its Fall River Division in the future. The Petitioners have chosen to defer rate relief until a future date, and have repeatedly represented that Southern Union's shareholders would bear any risk that the benefits and cost savings resulting from the merger may be insufficient to offset the acquisition premium (Petitioners Brief at 11; Tr. at 40-41). The Petitioners have voluntarily undertaken the risk of deferring the acquisition premium and transaction costs in the event they fail, in the future, to make the requisite showing of "countervailing advantages" required by Mergers and Acquisitions at 19. This feature of the merger proposal is of the Petitioners' own choosing and not at the Department's insistence. Thus, the Department finds that Fall River's ratepayers are likely to be better off, and certainly no worse off, than they would be absent the merger because the Petitioners are not seeking current recovery of any merger-related costs.

### 3. Gas-Cost Savings

#### a. Introduction

The Petitioners submit that approval of the merger will likely yield two primary benefits relating to gas supply functions. First, the Petitioners assert that Fall River's overall system reliability will increase as a result of the ability to plan, contract, and dispatch gas supply resources on an integrated basis (Exhs. SUFR-4, at 4-5; DTE 2-9, DTE 2-52). Second, the Petitioners assert that gas-cost savings will occur as a result of the more efficient utilization of peak-shaving facilities and peaking supply contracts (Exh. SUFR-4, at 3). The Petitioners did not venture to quantify the potential savings that could be achieved as a result of the coordination of the gas supply resources (Tr. at 97-98).

#### b. Analysis and Findings

In recently approved mergers and acquisitions, the Department has reaffirmed the importance of cost savings by utility companies and expected all utilities to explore any and all measures that provide the opportunity for these savings. Eastern-Essex Acquisition at 26; NIPSCO-Bay State Acquisition at 26, citing Mergers and Acquisitions at 18. The Department further stated that mergers and acquisitions are a useful and potentially beneficial mechanism for utility companies to consider in meeting their service obligations. Mergers and Acquisitions at 18. The Department here evaluates whether the opportunity exists for the Petitioners to achieve the savings described in the proposal while maintaining the level of service and reliability Fall River customers have experienced.

The Department concurs with the Petitioners that the proposed merger has the potential to provide customers gas cost savings (albeit of indeterminate size) resulting from the joint management and procurement of Southern Union's and Fall River's gas supplies, which in turn would result in greater economies and efficiencies (Exhs. SUFR-4, at 3-11; DTE 2-9, DTE 2-52; Tr. at 116). Thus, with respect to gas costs, the Department finds that Fall River's ratepayers are likely to be better off, and certainly no worse off, than they would be absent the merger. NIPSCO-Bay State Acquisition at 27.

## B. Quality of Service

### 1. Petitioners Proposal

The Petitioners propose to implement service quality measures to ensure that there is no degradation in service quality as a result of the merger (Exh. SUFR-3, at 10-12).<sup>(12)</sup> The Petitioners propose to track service quality performance in the areas of: (1) emergency, billing and service telephone call answering time; (2) response to emergency calls; (3) lost-time accidents; (4) service appointments met on the day scheduled; and (5) actual meter reads (Exh. SUFR-3, at 11). Because adequate historical data exists only for responses to emergency calls and lost-time accidents, the Petitioners request 18 months to implement the necessary systems and processes which will be used to track the remaining measures (Exh. DTE 2-29). At that time, the Petitioners propose to implement the systems and processes to track the service quality data and to submit such data to the Department for its review, consistent with the Department's decision in Eastern-Essex Acquisition at 32-34. The Petitioners state that their proposed service quality measures and implementation period are consistent with those implemented in Eastern-Essex Acquisition (Petitioners Brief at 6).

### 2. Analysis and Findings

The Department retains oversight of a company's service quality pursuant to G.L. c. 164, § 76, and has stated that a service quality index is an important bulwark against deterioration in a company's service to its customers. Eastern-Essex Acquisition at 32-33; D.P.U./D.T.E. 97-63, at 15 (1998); Mergers and Acquisitions, D.P.U. 93-167-A at 8-10 (1994). The Petitioners have proposed to increase the number of service functions to be tracked and reported to the Department, as well as implement workforce automation

programs intended to provide customers with greater service convenience (Exh. SUFR-1, at 8; Tr. at 28-31). The Department finds that this increased effort by Southern Union, as the surviving company, is likely to improve service quality for Fall River's ratepayers. To ensure that there will be no reduction in the quality of service following consummation of the merger, the Department directs the Petitioners to implement their proposed service plan and to be prepared to submit for review by the Department an acceptable service quality plan 18 months after closing, or in accordance with any directives prescribed as a result of the Department's ongoing investigation into service quality, docketed as D.T.E. 99-84.

### C. Societal Costs

#### 1. Petitioners Proposal

The Petitioners represented there will be no reduction in the labor force as a result of the merger (Exh. SUFR-2, at 22-23; Tr. at 34-35). In fact, the Petitioners expect the merger to have a positive impact on economic development in the Fall River area (*id.*). Specifically, the Petitioners maintain that future developments in the gas business, including increased customer demands and new technologies, will increase the need for a qualified workforce (Exh. SUFR-2, at 23; Petitioners Brief at 17). Moreover, the Petitioners represented that Southern Union will maintain a local management presence in the Fall River Division, which will remain responsible for day-to-day operations (Exh. SUFR-3, at 23; Tr. at 38-39).

#### 2. Analysis and Findings

The impact of mergers on employment levels is an important matter for the Department's consideration and review. See Eastern-Essex Acquisition at 44. Although job redundancies in consolidated systems would impose avoidable costs and thus would be detrimental to ratepayers, the Department has noted that the elimination of these redundancies should be accomplished in a way that mitigates the effect on the utility's employees. Eastern-Essex Acquisition at 43. The Department has stated that proponents of mergers must demonstrate that they have a plan to minimize the effect of job displacement on employees. Eastern-Essex Acquisition at 44. The Petitioners anticipate no layoffs due to the impending merger. Further, Southern Union has committed itself to maintaining a local presence in Fall River. Accordingly, the Department finds that the proposed merger will have no negative effects on employment.

### D. Acquisition Premium

#### 1. Petitioners Proposal

The Petitioners estimate that the merger would result in an acquisition premium of approximately \$36,950,000 (Exh. DTE 2-13). The acquisition premium is primarily based on the purchase price of \$23.50 per-share book-value<sup>(13)</sup> of Fall River's assets and on the number of Fall River shares anticipated to be outstanding as of the consummation

of the merger (Exhs. SUFR-2, at 3, 16; DTE 2-13).<sup>(14)</sup> The Petitioners propose to allocate the acquisition premium proportionately among Southern Union and its operating divisions after consummation of the merger (Exhs. DTE 2-2; DTE 2-20). The actual calculation would be based on a review of Fall River's accounts, operations, and the final costs of the transaction (Exh. SUFR-2, at 16). The Petitioners propose to amortize the acquisition premium over a period not exceeding forty years, consistent with GAAP under purchase accounting (Tr. at 40-41; 45-46).<sup>(15)</sup>

## 2. Analysis and Findings

The Department has stated that it will consider individual merger or acquisition proposals that seek recovery of an acquisition premium, as well as the recovery level of such premiums. NIPSCO-Bay State Acquisition at 39, Eastern-Essex Acquisition at 61, citing Mergers and Acquisitions at 18-19. Under the Department's standard, a company proposing a merger or acquisition must demonstrate that the costs or disadvantages of the transaction are accompanied by benefits that warrant their allowance. Thus, allowance or disallowance of an acquisition premium would be just one part (albeit an important one) of the cost/benefit analysis under the § 96 standard. Id.

With respect to the level of consideration paid by Southern Union for Fall River, the record evidence demonstrates that the purchase price was evaluated in light of a comparison with purchase prices associated with other recent mergers and acquisitions by other LDCs, and an assessment of the potential long-term benefits (Exh. SUFR-2, at 5). A purchase price at a multiple of book value expresses a buyer's expectations of the acquired company's future contributions to combined operations. NIPSCO-Bay State Acquisition at 43-44; Eastern-Essex Acquisition at 64. The particular exchange rate involved in merger or acquisition stock transactions expresses a number of matters of value to the buyer, including a premium for management control and long-term strategic and economic value perceived by the buyer as accruing from the transaction. Id. Between 1997 and 1999, acquisition prices in natural gas distribution company mergers have ranged from 2.2 times and 3.1 times the book value of the acquired company, with an average price of 2.7 times book value (Exh. SUFR-2, Att. 2; RR-DTE-2). Southern Union, as a knowledgeable and willing buyer, experienced in other acquisitions, was prepared to pay a premium over Fall River's book value in exchange for long-term growth potential and to accept the risk associated with justifying, or not, the recovery of this premium at a later date (Exh. SUFR-2, at 5-6; RR-DTE-2).

The proposed purchase price for Fall River's stock represents a premium of 2.8 times book value (Exh. SUFR-2, at 5). The price paid by Southern Union for Fall River in this case is well within the range of what has been offered in other transactions involving natural gas distribution companies (Exh. SUFR-2, Att. 2; RR-DTE-2).<sup>(16)</sup> The premium lies within the historic range and has been validated by the market at large. The Department finds that the proposed purchase price for Fall River's common stock and proposed exchange ratio is in line with other Department-approved gas acquisitions and, therefore, is reasonable and represents a valid expression of today's market conditions.

The Petitioners propose to amortize the acquisition premium over a period not exceeding forty years using the purchase accounting method.<sup>(17)</sup> While mergers and transactions can also be accounted for using pooling of interests accounting, both GAAP and the Securities and Exchange Commission ("SEC") require that a business combination must satisfy 12 conditions to use pooling of interests accounting; and failure to satisfy even one of these conditions would require the combination to be recorded through purchase accounting. NIPSCO-Bay State Acquisition at 40. In view of the stringent requirements for the use of pooling-of-interests accounting and the SEC's preference for purchase accounting, the Department concludes that the use of purchase accounting for the proposed merger complies with GAAP. Accordingly, the Department finds that the Petitioners' proposed use of purchase accounting to record the merger is appropriate.

Moreover, the Department finds that the merger has been structured so that Fall River's ratepayers are not at risk for recovery of any acquisition premium or merger-related costs. In fact, the Petitioners have represented that Southern Union's shareholders would bear any risk in the event that the benefits and cost savings resulting from the merger would be insufficient to offset the acquisition premium (Exhs. SUFR-2, at 18; DTE-2-23; Tr. at 11-12, 41-43; Petitioners Brief at 6).

With respect to the amortization period of the acquisition premium, the Department has historically recognized that any acquisition premium would be, in general, amortized over the life of the acquired assets. Mergers and Acquisitions at 12, citing Bay State Gas Company, D.P.U. 17726, at 5-6 (1973), Boston Gas Company, D.P.U. 17574, at 11 (1973), Boston Gas Company, D.P.U. 17138, at 7-8 (1971). The record evidence in this proceeding indicates that the Petitioners propose to use rules established by GAAP in calculating the amortization period of the acquisition premium (Tr. at 40-42). The Department concludes that the amortization period of 40 years complies with the rules established by GAAP and Department precedent.

Based on the evidence, the Department finds that the acquisition premium of \$36.95 million as estimated by the Petitioners fairly represents the total acquisition premium that will result from the merger. Because the stock exchange would be based on the actual number of Fall River shares outstanding on the consummation date, as well as Southern Union's stock price applied in the merger agreement, the actual amount of the acquisition premium cannot be precisely calculated until the consummation date or shortly thereafter -- although its range is determined through a formula. The Petitioners are directed to provide the Department with a copy of the journal entries or a schedule summarizing such entries upon completion of the merger, in sufficient detail so as to determine the actual acquisition premium. Additionally, the Petitioners are directed to provide the Department with a detailed listing of the final transaction costs 90 days from the date of consummation of the merger.

#### E. Financial Integrity of Post-Merger Company

##### 1. Petitioners Proposal

The Petitioners contend that the proposed merger will have no adverse effects on the financial integrity of Southern Union's Fall River Division, and will provide the Fall River Division with greater access to capital than is now available to that company (Exh. SUFR-2, at 20). Specifically, the Petitioners explain that because Fall River will be joining a \$2.5 billion company, which will serve approximately 1.6 million customers, Fall River's operations will enjoy greater financial stability and flexibility which will lead to cost savings over time, because, among other things, of the ability to obtain financing on more favorable terms and conditions (Exh. SUFR-2, at 20).

Additionally, the Petitioners maintain that the proposed merger will strengthen the financial integrity of Southern Union as a whole, because the merger will expand Southern Union's geographic diversity and minimize the effects of adverse economic or weather conditions in any one region (Exh. SUFR-1, at 9). This, according to the Petitioners, will have the effect of minimizing Southern Union's short-term risk and enhancing its long-term financial strength (Exhs. SUFR-1, at 9, 20; DTE 2-45, DTE 2-49; Tr. at 61-62).

## 2. Analysis and Findings

If the merger is implemented, Fall River (a gas company within the meaning of

G.L. c. 164, § 1, and a Massachusetts corporation) would merge into Southern Union, an existing multistate gas distribution company incorporated in Delaware. The merger would thus extinguish Fall River's corporate existence under Massachusetts law, and convert Fall River into an operating division of Southern Union.

The Department has stated that the financial integrity of a company may be one of the factors considered in evaluating a merger petition. Mergers and Acquisitions at 8-9. A review of Southern Union's financial and operating data, contained in its annual reports to both the Federal Energy Regulatory Commission and the Securities and Exchange Commission, and the annual returns and disclosure statements provided to its shareholders, demonstrates that Southern Union is also financially viable (Exhs. SUFR-6; SUFR-7; SUFR-8). Moreover, Fall River's post-merger financial position is likely to improve because of the additional sources of capital that will be available as a result of its affiliation with Southern Union. Such an improvement would likely result in benefits to ratepayers. Accordingly, the Department finds that the merger will not adversely affect Fall River's or Southern Union's financial integrity.

## F. Effect on Competition and Economic Development

### 1. Petitioners Proposal

The Petitioners contend that the proposed merger will not adversely affect competition in the gas industry (Exh. SUFR-2, at 21-22). The Petitioners state that Southern Union has a history of promoting customer choice and unbundling initiatives, which support competition in the gas industry (Exh. SUFR-2, at 21-22; Petitioners Brief at 15).

## 2. Analysis and Findings

The record indicates that Southern Union has participated in federal and state proceedings concerning the development of open-access gas transportation and unbundling (Exh. SUFR-2, at 21-22). Moreover, Southern Union has stated that its entry into Massachusetts, by virtue of the proposed merger, will require investment in additional technology and produce additional benefits to customers through increased choice and education (Exh. SUFR-2, at 21-22; Tr. at 28-32). Accordingly, the Department finds that the proposed merger will not adversely affect competition in the gas industry.

### G. Cost Allocation Issues

#### 1. Petitioners Proposal

The Petitioners state that they are not seeking approval of either a joint and common cost model or a specific allocation method as part of this merger (Tr. at 9). Instead, the Petitioners propose to submit for Department approval, in a future rate proceeding, a joint and common cost model outlining the underlying method and procedures for the assignment of joint and common costs among Southern Union's operating divisions and subsidiaries (Exh. DTE 2-19; Tr. at 25-27). Southern Union states that it will rely on its experience in developing and supporting cost allocations to its multiple regulators to create an allocation method in Fall River's next rate proceeding (Exh. SUFR-2, at 12).<sup>(18)</sup>

#### 2. Analysis and Findings

In determining whether rates are just and reasonable, the Department may examine affiliate transactions to ensure that dealings between affiliated companies provide direct benefits to ratepayers and that associated costs are reasonable and allocated in a nondiscriminatory manner. G.L. c. 164, § 76A; NIPSCO-Bay State Acquisition at 46; Cambridge Electric Light Company, D.P.U. 92-250, at 78 (1993); Bay State Gas Company, D.P.U. 92-111, at 134-135 (1992). The Department historically has exercised its obligation and authority to ensure that a company's affiliate costs passed on to the company's ratepayers are reasonable and that ratepayers pay no more than a fair portion of the costs. NIPSCO-Bay State Acquisition at 46; D.P.U. 92-111, at 136-137; New England Telephone and Telegraph Company, D.P.U. 86-33-G at 113-211 (1989); Oxford Water Company, D.P.U. 1699, at 10-13 (1984) ("D.P.U. 1699").

The Department's standard for reviewing affiliate transactions was articulated in D.P.U. 1699. In that case, the Department found that to recover costs incurred from an affiliate, a company must show that those costs: (1) are specifically beneficial to the individual company seeking rate relief (as opposed to other subsidiary members of the system as a whole); (2) reflect a reasonable and competitive price; and (3) are allocated by a formula that is cost-effective and nondiscriminatory. D.P.U. 1699, at 13. The Department has previously noted the desirability of direct assignment of costs where possible. Berkshire Gas Company, D.P.U. 90-121, at 58-59 (1990). In the case of indirect common costs, which are not amenable to direct assignment, the Department has required the use of cost



allocations that are appropriate to the particular cost that is being allocated between companies. Id. at 64-70. See also Massachusetts-American Water Company, D.P.U. 95-118, at 101 (1996); South Egremont Water Company, D.P.U. 94-161, at 3 n.3 (1995). More recently, the Department has elaborated on this policy, noting that services should be provided to an affiliate at fully allocated costs, and that cost allocation methods ensure that all direct costs and a portion of indirect costs are recovered from the affiliate. D.P.U./D.T.E. 97-96, at 7 (1998).

Accordingly, the Petitioners are hereby directed to develop a cost allocation system for transactions among Southern Union's respective divisions consistent with Department precedent.

#### H. Fall River Operating as a Division of Southern Union

##### 1. Introduction

Southern Union is a natural gas local distribution company, incorporated in Delaware with a principal place of business in Austin, Texas (Exh. SUFR-1, at 2). After the merger, Southern Union will conduct Fall River's gas utility business as an operating division within Southern Union's New England Business Unit (Exhs. SUFR-1, at 10-11; DTE 2-35, DTE 2-37). The Petitioners state that the Fall River-Southern Union proposal differs from other merger proposals considered by the Department in that Southern Union operates as a single utility in multiple jurisdictions (Exhs. SUFR-1, at 2-3, 10-11; SUFR-2, at 6-7; DTE 2-35; Tr. at 20-24). The Petitioners state that the Fall River Division of Southern Union would remain fully subject to the Department's regulatory jurisdiction under G.L. c. 164 (Exh. DTE 2-2).

##### 2. Standard of Review

In pertinent part, G.L. c. 164, § 8A, requires the Department, after notice and public hearing, to certify to the secretary of state that the public convenience will be promoted, permitting Southern Union to operate as a gas company in Massachusetts. Because the statute does not define "public convenience," the Department relies on our precedents relating to "public convenience and necessity."

The Department has been accorded wide discretion in determining whether the "public convenience and necessity" would be promoted by some proposed action. Zacks v. Department of Public Utilities, 460 Mass. 217 (1985) Almeida Bus Lines, Inc. v. Department of Pub. Utils., 348 Mass 331 (1965); Holyoke St. Ry. v. Department of Pub. Utils., 347 Mass. 440 (1964); Newton v. Department of Pub. Utils., 339 Mass. 535 (1959). "Public convenience and necessity" is a term of art that the courts have equated with "public interest." Zacks v. Department of Public Utilities, 460 Mass. 217, 223 (1985). Therefore, to determine whether to authorize a gas company merger, the Department will consider whether the requested action is in the public interest. See, e.g., NIPSCO-Bay State Acquisition, D.T.E. 98-31, at 57.

Additionally, G.L. c. 164, § 5A requires a gas or electric corporation operating in Massachusetts to include the words "gas company" or "electric company," depending upon the particular company, in its name. The statute also prohibits any gas or electric corporation operating in Massachusetts from assuming the name or trade name of (1) another corporation established under the laws of the Commonwealth, or (2) of a corporation wherever established, firm, association, or person carrying on business in the Commonwealth, or (3) any such name within three years prior thereto, or (4) any such name under reservation under the laws of the Commonwealth for another or proposed corporation wherever established, or (5) any name so similar to the existing corporation that as to be likely to be mistaken for it. Notwithstanding the foregoing, a name or trade name can be assumed with the written consent of the company previously filed with the secretary of state.

### 3. Analysis and Findings

#### a. Jurisdictional Issues

The entrance of foreign corporations in the Massachusetts gas and electric industries previously raised concerns over the legal status of foreign corporations operating gas and electric systems within Massachusetts; and foreign ownership was not favored. Third Annual Report of the Board of Gas and Electric Light Commissioners, at 58 (1888). The enactment of the Electric Restructuring Act<sup>(19)</sup> ("Act") revised the definition of a "gas company" or "electric company" set out in G.L. c. 164, § 1, to include non-Massachusetts corporations operating gas or electric utilities within Massachusetts.<sup>(20)</sup> The Act gives the Department the same jurisdiction over foreign utilities operating in Massachusetts as is currently applied to Massachusetts-chartered corporations. Therefore, there is no longer a bar on "foreign" corporations operating gas or electric systems within Massachusetts. The Department considers that approval of Southern Union's merger with Fall River and the request to conduct Fall River's gas utility business as an operating division of Southern Union to be consistent with the public interest (Exhs. DTE 2-35, DTE 2-37). Because Southern Union's Fall River Division would remain fully subject to the Department's regulatory jurisdiction under G.L. c. 164, this proposal is consistent with the public interest (Exh. DTE 2-2). Because the courts have equated "public interest" with "public convenience," for the reasons described above, the Department finds that the public convenience would be promoted by authorizing Southern Union to operate as a gas company in Massachusetts. NIPSCO-Bay State Acquisition at 62.

Southern Union's current articles of incorporation authorize it to conduct business in any state or territory of the United States, as well as in foreign countries (Exh. DTE 2-39). Therefore, the Department concludes that Southern Union has complied with the requirements of G.L. c. 164, § 8A, and finds that approval may be granted. As a condition of this approval, the Petitioners are directed to submit to the Department written evidence that Southern Union has filed its articles of incorporation with the secretary of state. Southern Union shall not commence operations in Massachusetts until such a filing has been made in satisfactory form to the secretary of state. The Department places the Petitioners on notice that Southern Union's authorization to operate as a gas company in

Massachusetts shall expire in 60 days from the date of this order, unless the merger is consummated on or before that date. NIPSCO-Bay State Acquisition at 62.

b. Corporate Name

Southern Union's present corporate name does not conform to the requirements of G.L. c. 164, § 11. The Petitioners indicated that, if the merger is ultimately implemented, Southern Union would operate in the Fall River Division under a d/b/a arrangement as "Fall River Gas Company," in order to maintain name identification with Fall River customers and thereby avoid customer confusion (Tr. at 22-23).<sup>(21)</sup>

G.L. c. 156B, § 11, in relevant part, permits corporations to assume any name that has not been used by a corporation in current operation or had been in operation during the prior three years, unless written consent of the preexisting corporation is filed with the state secretary. General Laws c. 164, § 5A imposes identical requirements on the assumption of a name by a gas or electric company, and makes additional provision for the use of trade names. Based on a review of G.L. c. 156B and c. 164, the Department concludes that there is no statutory bar against the use of an assumed name by Southern Union, and that an assumed name which conforms to the requirements of G.L. c. 164, § 5A would bring Southern Union into compliance with the requirements of that statute. Furthermore, the Department considers that the continued use of the Fall River corporate name by Southern Union for its Fall River Division would reduce the possibility of customer confusion resulting from the merger. Accordingly, the Department finds it appropriate for Southern Union to operate under Fall River's name when the merger is consummated.

V. STOCK ISSUANCE

A. Introduction

Under the terms of the Merger Agreement, Fall River shareholders would receive, for each share of Fall River common stock, a combination of Southern Union common stock ("Stock Consideration") or cash equivalent to \$23.50 per share for Fall River stock ("Cash Consideration") (Exhs. SUFR-2, at 3; SUFR-4, at 10). The Merger Agreement requires that at least 50 percent of the approximately 2,206,034 shares of Fall River common stock anticipated to be outstanding as of the consummation of the merger be converted into Southern Union common stock (Exhs. SUFR-2, at 3; SUFR-4, at 10; Tr. at 70). Fall River shareholders can elect to receive Southern Union common stock, cash, or a combination of stock and cash, subject to proration and a formula based on the average trading price of Southern Union common stock during a ten-day trading period that ends three trading days prior to the close of the merger (Exhs. SUFR-2, at 3; SUFR-4, at 10-14).

B. Standard of Review

In order for the Department to approve the issuance of stock, bonds, coupon notes, or other types of long-term indebtedness<sup>(22)</sup> by an electric or gas company, the Department

must determine that the proposed issuance meets two tests. First, the Department must assess whether the proposed issuance is reasonably necessary to accomplish some legitimate purpose in meeting a company's service obligations, pursuant to G.L. c. 164, § 14. Fitchburg Gas & Electric Light Company v. Department of Public Utilities, 395 Mass. 836, 842 (1985) ("Fitchburg II"), citing Fitchburg Gas & Electric Light Company v. Department of Public Utilities, 394 Mass. 671, 678 (1985) ("Fitchburg I"). Second, the Department must determine whether the Company has met the net plant test.<sup>(23)</sup> Colonial Gas Company, D.P.U. 84-96 (1984).

The Court has found that, for the purposes of G.L. c. 164, § 14, "reasonably necessary" means "reasonably necessary for the accomplishment of some purpose having to do with the obligations of the company to the public and its ability to carry out those obligations with the greatest possible efficiency." Fitchburg II at 836, citing Lowell Gas Light Company v. Department of Public Utilities, 319 Mass. 46, 52 (1946). In cases where no issue exists about the reasonableness of management decisions regarding the requested financing, the Department limits its Section 14 review to the facial reasonableness of the purpose to which the proceeds of the proposed issuance will be put. Canal Electric Company, et al., D.P.U. 84-152, at 20 (1984); see, e.g., Colonial Gas Company, D.P.U. 90-50, at 6 (1990).

The Fitchburg I and II and Lowell Gas cases also established that the burden of proving that an issuance is reasonably necessary rests with the company proposing the issuance, and that the Department's authority to review a proposed issuance "is not limited to a 'perfunctory review.'" Fitchburg I at 678; Fitchburg II at 842, citing Lowell Gas at 52.

Where issues concerning the prudence of a company's capital financing have not been raised or adjudicated in a proceeding, the Department's Order may not in any way be construed as ruling on the appropriate ratemaking treatment to be accorded any costs associated with the proposed financing. See, e.g., Boston Gas Company, D.P.U. 95-66, at 7 (1995).

Regarding the net plant test, a company is ordinarily required to present evidence that its net utility plant (original cost of capitalizable plant less accumulated depreciation) is equal to or exceeds its total capitalization (the sum of its long-term debt, preferred stock, and common stock outstanding) and will continue to do so after the proposed issuance.

D.P.U. 84-96, at 5. If the Department determines at that time that the fair structural value of the net plant and land and the fair market value of the nuclear or fossil fuel inventories owned by the company are less than its outstanding debt and stock, it may prescribe such conditions and requirements as it deems best to make good within a reasonable time the impairment of the capital stock. G.L. c. 164, § 16.

### C. Analysis and Findings

The Petitioners request authority to issue stock in order to establish the framework within which the merger could be consummated. Without the authority to issue the stock, Fall

River's stock exchange with Southern Union could not take place, and this merger would not take place. Therefore, the Department finds that the issuance of common stock by Southern Union of approximately 2,206,234 shares is a necessary mechanism for the purpose of effecting the proposed merger. Accordingly, the Department finds that the proposed stock issuance is reasonably necessary and is in accordance with G.L. c. 164, § 14.

With regard to the net plant test requirement of G.L. c. 164, § 16, upon review of the financial statements of Southern Union and Fall River, the Department concludes that the Company's total stock and long-term debt will not exceed the Company's net plant after the issuance of the additional shares of common stock (Exhs. SUFR-8, at 22, 40-41; DTE 2-7, at 4-5). The Department determines that the issuance results in a fair structural value of the Southern Union's plant being less than the outstanding securities. Therefore, the Department finds that the proposed issuance of common stock adheres to the principles and conditions under § 16.

For a number of years, Southern Union has implemented a policy of distributing, in lieu of cash dividends, an annual common stock dividend of five percent to its common stockholders (Exh. SUFR-5 (1999 Annual Report), at 16). G.L. c. 164, § 11, prohibits a gas or electric company from declaring any stock dividend or dividing the proceeds of the sale of stock among its shareholders, and requires the payment of cash before any new stock may be issued. Thus, Southern Union's practice, if continued, would be in direct contravention of Massachusetts law. The Department expects Southern Union to comply with all Massachusetts general laws and directs Southern Union to cease its stock dividend policy immediately. We note that failure to comply with G.L. c. 164, § 11 and the Department's directives will result in the voiding of all common stock certificates issued by Southern Union for the purpose of issuing common stock dividends, and render Southern Union's directors and officers liable for penalties as provided in G.L. c. 164, §§ 12 and 17.

## VI. ORDER

Accordingly, after due notice, hearing and consideration, it is

ORDERED: That pursuant to G.L. c. 164, § 96, the merger of Fall River Gas Company into Southern Union Company is hereby approved, subject to the filing of certification that the shareholders of both Fall River Gas Company and Southern Union Company have voted two-thirds in the affirmative as required by G.L. c. 164, §96; and it is

FURTHER ORDERED: That the Department hereby approves for Southern Union Company the issuance of up to 2,206,234 shares of common stock, to be offered at not less than par; and it is

FURTHER ORDERED: That it is confirmed that, upon consummation of the merger of Fall River Gas Company and Southern Union Company, Southern Union Company shall have all rights, powers, privileges, franchises, properties, real, personal or mixed, and

immunities to engage in all activities in all the cities and towns in which Fall River Gas Company was engaged in immediately prior to the merger, and that further action pursuant to G.L. c. 164, § 21 is not required to consummate the merger of Fall River Gas Company and Southern Union Company; and it is

FURTHER ORDERED: That a copy of the journal entries, or a schedule summarizing such entries, recording the effect of the merger shall be filed with the Department upon consummation of the merger; and it is

FURTHER ORDERED: That the Petitioners shall comply with all directives contained in this Order.

By Order of the Department,

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James Connelly, Chairman

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W. Robert Keating, Commissioner

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Paul B. Vasington, Commissioner

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Eugene J. Sullivan, Jr., Commissioner

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Deirdre K. Manning, Commissioner

Appeal as to matters of law from any final decision, order or ruling of the Commission may be taken to the Supreme Judicial Court by an aggrieved party in interest by the filing of a written petition praying that the Order of the Commission be modified or set aside in whole or in part.

Such petition for appeal shall be filed with the Secretary of the Commission within twenty days after the date of service of the decision, order or ruling of the Commission, or within such further time as the Commission may allow upon request filed prior to the expiration of twenty days after the date of service of said decision, order or ruling. Within ten days after such petition has been filed, the appealing party shall enter the appeal in the Supreme Judicial Court sitting in Suffolk County by filing a copy thereof with the Clerk of said Court. (Sec. 5, Chapter 25, G.L. Ter. Ed., as most recently amended by Chapter 485 of the Acts of 1971).

1. <sup>1</sup> Southern Union has also petitioned for approval of a merger with North Attleboro Gas Company ("North Attleboro") by virtue of a proposed merger with Providence Energy, a Rhode Island-based holding company which directly owns the common stock of both North Attleboro and Providence Gas Company, along with Valley Resources, a second Rhode Island-based holding company which owns the common stock of two other Rhode Island LDCs. That proceeding has been docketed as D.T.E. 00-26.

2. <sup>2</sup> The Petitioners' request for approval of the merger is unopposed. On June 2, 2000, the Petitioners and the Attorney General notified the Department that the Attorney General had no objection to the Department granting the relief requested by the Petitioners (Tr. at 17-18).

3. <sup>3</sup> The evidentiary hearing in this proceeding was conducted in conjunction with the evidentiary hearing in Southern Union-North Attleboro Merger, D.T.E. 00-26.

4. <sup>4</sup> Southern Union intends to conduct Fall River's gas utility business as part of a "New England Business Unit" formed to operate Southern Union's Massachusetts and Rhode Island operations, under the name "Fall River Gas Company" (Petition at 2; Exh. SUFR-1, at 10).

5. <sup>5</sup> The Petitioners state that the "Minimum Value" exchange ratio of \$16.875 and the "Maximum Value" exchange ratio of \$19.6875 is a range set at ten percent below and five percent above respectively, the \$18.75 closing price of Southern Union's stock as of October 1, 1999 (Exh. DTE-2-12). The parameters of the exchange ratios were established through negotiations between Southern Union and Fall River (Exh. DTE 2-12). The Petitioners explained that setting an exchange ratio range eliminates some of the risk involved for both parties in a merger (Exhs. DTE 2-12; DTE 4-11).

6. <sup>6</sup> The Merger Agreement requires that at least 50 percent of the approximately 2.2 million shares of Fall River common stock be converted into Southern Union common stock (Exhs. SUFR-2, at 3; DTE 2-13).

7. <sup>7</sup> The Petitioners state that, to the extent that merger-related savings materialize in the future, these savings will help to offset any future rate increases required for Fall River (Exh. SUFR-2, at 19).

8. <sup>8</sup> The Department notes that a finding that a proposed merger or acquisition would probably yield a net benefit does not mean that such a transaction must yield a net benefit to satisfy G.L. c. 164, § 96 and Boston Edison, D.P.U. 850.

9. <sup>9</sup> Thus, Merger and Acquisitions removed the per se bar to recovery of acquisition premiums and treated them as just another kind of costs to be reckoned in the balancing of costs and benefits required by G.L. c. 164, § 96 and Boston Edison Company, D.P.U. 850.



10. <sup>10</sup> The Petitioners calculated the \$2,000,000 using the analysis that the Fall River presented in its previous base rate case, Fall River Gas Company, D.P.U. 96-60 (1996) (Exh. DTE 2-4).

11. <sup>11</sup> Fall River's recent rate case history is as follows: (1) Fall River Gas Company, D.P.U. 750 (1981) (\$1.3 million increase); (2) Fall River Gas Company, D.P.U. 1557 (1983) (\$1.7 million increase); (3) Fall River Gas Company, D.P.U. 91-60 (1991) (\$2.7 million increase); (4) Fall River Gas Company, D.P.U. 96-60 (1996) (\$3.2 million increase).

12. <sup>12</sup> On October 29, 1999, the Department opened an investigation to establish guidelines for service quality standards for both electric companies and LDCs; this proceeding has been docketed as D.T.E. 99-84.

13. <sup>13</sup> The purchase price of \$23.50 per share was the result of negotiations between Southern Union and Fall River (Exhs. DTE 2-10; DTE 2-11; DTE 2-12).

14. <sup>14</sup> The acquisition premium is a function of the purchase price of \$23.50 per share, the book value as of December 31, 1999, and the approximately 2,206,234 shares that the Petitioners estimate will be outstanding as of the consummation of the merger (Exh. DTE 2-13). The Petitioners then added the total estimated transaction costs of approximately \$3,000,000 to the \$51,846,499 purchase price for Fall River's common stock to derive the total estimated purchase price of \$54,846,499 (Exh. DTE 2-13). Subtracting the book value of approximately \$17,896,439 from the total purchase price of \$54,846,499 results in the \$36,950,060 acquisition premium (Exh. DTE 2-13).

15. <sup>15</sup> As noted in Section II.C, above, the Petitioners are not seeking recovery of the acquisition premium or merger-related costs through base rates in this proceeding.

16. <sup>16</sup> Southern Union stated that it did not engage the services of an investment banker in conjunction with negotiating the merger. Instead, Southern Union relied on its own analysis of Fall River, its knowledge of the consideration involved in recent gas industry acquisitions, and conversations with investment analysts in determining the price that Southern Union was willing to pay for the properties (Exhs. DTE 2-11; DTE 4-7; Tr. at 51-52; RR-DTE-3).

17. <sup>17</sup> The Petitioners indicated that if pooling of interests accounting was used for the transaction, Southern Union would be precluded from engaging in any business combinations for a period of two years (Tr. at 84-85). Further, Southern Union's decision not to use pooling of interests accounting to record the acquisition premium is based on its historical experience with past merger transactions (Tr. at 84-85).

18. <sup>18</sup> The Petitioners submitted a copy of Southern Union's corporate cost allocation report, Assignment and Allocation of Costs of Joint and Common Costs, Review of Use of Causal Pools. Southern Union states that it uses this method for allocating joint and

common costs as a basis for developing a model each time it files a general rate case (Exh. DTE 2-19).

19. <sup>19</sup> An Act Relative to Restructuring the Electric Utility Industry in the Commonwealth, Regulating the Provisions of Electricity and Other Services, and Promoting Enhanced Consumer Protection Therein. St. 1997, c. 164.

20. <sup>20</sup> Section 189 of St. 1997, c. 164 changed the definition of "gas company" and "electric company" found in G.L. c. 164, § 1, so that a gas or electric company need not be a domestic Massachusetts corporation, provided such corporation is organized for the purpose of making and selling, or distributing and selling, gas and electricity within Massachusetts.

21. <sup>21</sup> In addition to the Fall River Division, Southern Union would also be operating a North Attleboro Division in Massachusetts resulting from the proposed merger of North Attleboro Gas Company's parent corporation, Providence Energy, with Southern Union. That proceeding has been docketed as D.T.E. 00-26. See Section I, above.

22. <sup>22</sup> Long-term refers to periods of more than one year after the date of issuance.

G.L. c. 164, § 16.

23. <sup>23</sup> The net plant test is derived from G.L. c. 164, § 16.